EX PARTE OR LATE FILED



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Timothy M. Boucher Corporate Counsel

REDACTED - FOR PUBLIC INSPECTION

ORIGINAL

Via Courier

EXPARTE

September 6, 2007

Ms. Marlene H. Dortch, Secretary Federal Communications Commission 445 12th Street, S.W. Washington, DC 20554 FILED/ACCE: D

SEP - 6 2007

Federal Communications Commission
Office of the Secretary

Re:

In the Matter of Petition of Qwest Corporation for Waiver of Depreciation Regulation Pursuant to 47 C.F.R. § 1.3 – WC Docket No. 05-259

Request for Confidential Treatment and Justification

Dear Ms. Dortch:

Qwest Corporation ("Qwest") requests confidential treatment of certain information contained in Attachment A to the appended *ex parte* Letter from Phil Grate being filed in the above-captioned waiver proceeding in response to questions from Federal Communications Commission ("Commission") staff. Qwest previously requested confidential treatment for the confidential information contained in Attachments G, H, I, K, L and the Worksheets in Attachment M and herein renews its request for confidential treatment of these Attachments (which each have attached to them the confidentiality requests/justifications that were included with the submissions when they were initially filed in this docket). Attachment A to the Grate Letter that includes confidential information (that is, the non-redacted version) has been marked "CONFIDENTIAL – NOT FOR PUBLIC INSPECTION". Attachments A, G, H, I, K, L and the Worksheets in Attachment M are also marked likewise (as previously submitted). Qwest requests that the non-redacted, confidential version of this *ex parte* be withheld from public inspection.

Qwest considers certain information contained in Attachment A to the Grate Letter -- pertaining to detailed data associated with GAAP depreciation and differences between GAAP depreciation and regulated depreciation data -- to be confidential. This information is confidential financial information that is "not routinely available for public inspection." As such, Qwest requests confidential treatment of this information and is filing a non-redacted version of the submission pursuant to both FCC rules 47 C.F.R. §§ 0.457(d) and 0.459. Pursuant to Commission rule, 47 C.F.R. § 0.459(b), Qwest provides justification for the confidential treatment of this information in the Appendix to this letter.

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Qwest is simultaneously submitting, under separate covers, both a confidential version of this *ex parte* including the Grate Letter and the confidential Attachments (as well as the non-confidential Attachments) and a redacted version of this *ex parte* including the Grate Letter and the redacted versions of the Attachments (as well as the non-confidential Attachments), which are marked "REDACTED - FOR PUBLIC INSPECTION", wherein the confidential information has been omitted. Both the redacted and non-redacted versions of the *ex parte* are being served on Staff of the Commission's Wireline Competition Bureau as indicated below.

Included with both the non-redacted and redacted submissions is the same copy of the Letter from Phil Grate, Director-State and Federal Relations, Qwest, to Ms. Marlene Dortch, Secretary, Federal Communications Commission, dated September 6, 2007, which contains *no* confidential information. As well, included with the non-redacted submission are the non-redacted responses to the questions of the Staff (Attachment A); included with the redacted submission are the redacted responses to the questions (Attachment A). For the non-redacted version, Qwest is submitting an original and one copy, along with a second copy to be stamped and returned to the courier. For the redacted version, Qwest is submitting an original and four copies, along with a fifth copy to be stamped and returned to the courier.

If you have any questions concerning this submission, please call me on 303-383-6608.

Sincerely,

/s/ Timothy M. Boucher

Attachment

Copy (via e-mail and hardcopy) to:

Albert Lewis (Albert, lewis@fcc.gov)

Donald Stockdale (Donald.stockdale@fcc.gov)

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Ms. Marlene H. Dortch September 6, 2007 Page 3 Redacted—For Public Inspection

APPENDIX

Confidentiality Justification

Qwest requests confidential treatment of certain information provided in Attachment A to the appended *ex parte* Letter from Phil Grate filed in response to questions from Federal Communications Commission ("Commission") staff because this information is confidential financial information that is not routinely made available for public inspection. Such information should be afforded confidential treatment under both 47 C.F.R. § 0.457(d) and § 0.459. All other appended attachments that contain confidential information continue to be covered by the confidentiality requests/justifications that were associated with these submissions when they were filed previously in WC Docket No. 05-259.

47 C.F.R. § 0.457(d)

Information contained in Attachment A of the Grate *ex parte* Letter is confidential and proprietary to Qwest as "commercial or financial information" under Section 0.457(d). Disclosure of such information to the public would risk revealing company-sensitive proprietary financial information. Therefore, in the normal course of Commission practice this information should be considered "Records not routinely available for public inspection."

47 C.F.R. § 0.459

Specific information in Attachment A is also subject to protection under 47 C.F.R. § 0.459, as demonstrated below.

Information for which confidential treatment is sought

Qwest requests that the information contained in Attachment A be treated on a confidential basis under Exemption 4 of the Freedom of Information Act. This information is competitively sensitive financial information which Qwest maintains as confidential and is not normally made available to the public. Release of the information could have a substantial negative competitive impact on Qwest. The confidential information is contained in the non-redacted version of Qwest's ex parte, which is marked with the following legend: **CONFIDENTIAL – NOT FOR PUBLIC INSPECTION**.

Commission proceeding in which the information was submitted

The information is being submitted In the Matter of Petition of Qwest Corporation for Waiver of Depreciation Regulation Pursuant to 47 C.F.R. § 1.3 – WC Docket No. 05-259.

Degree to which the information in question is commercial or financial, or contains a trade secret or is privileged

Ms. Marlene H. Dortch September 6, 2007 Page 4 Redacted- For Public Inspection

The financial information designated as confidential is commercial and financial information in the form of detailed data associated with GAAP depreciation and differences between GAAP and regulated depreciation data. As noted above, the data is commercially and financially-sensitive information which is not normally released to the public as such release could have a substantial negative competitive impact on Qwest.

Degree to which the information concerns a service that is subject to competition; and manner in which disclosure of the information could result in substantial competitive harm

The type of competitively sensitive financial information in Attachment A would generally not be subject to routine public inspection under the Commission's rules (47 C.F.R. § 0.457(d)), which demonstrates that the Commission already anticipates that the release of this kind of information likely would produce competitive harm. Qwest confirms that release of its confidential and proprietary information would cause it competitive harm by allowing its competitors to become aware of sensitive proprietary financial information regarding the operation of Qwest's business.

Measures taken by Qwest to prevent unauthorized disclosure; and availability of the information to the public and extent of any previous disclosure of the information to third parties

Qwest has treated and treats the information disclosed in its non-redacted *ex parte* as confidential and has protected it from public disclosure to parties outside of the company.

Justification of the period during which Qwest asserts that the material should not be available for public disclosure

Qwest cannot determine at this time any date on which this information should not be considered confidential or would become stale for purposes of the current inquiry, except that the information would be handled in conformity with general Qwest records retention policies, absent any continuing legal hold on the data.

Other information that Qwest believes may be useful in assessing whether its request for confidentiality should be granted

Under applicable Commission and court rulings, the information in question should be withheld from public disclosure. Exemption 4 of the Freedom of Information Act shields information that is (1) commercial or financial in nature; (2) obtained from a person outside government; and (3) privileged or confidential. The information in question satisfies this test.



Qwest

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Philip E. Grate

Director - State and Federal Relations

EX PARTE

Filing via courier

September 6, 2007

Marlene H. Dortch Secretary Federal Communications Commission 445 12th Street, S.W. Washington, DC 20554

Re:

In the Matter of Petition of Qwest Corporation for Waiver of Depreciation Regulation Pursuant to 47 C.F.R. § 1.3 – WC Docket No. 05-259

Dear Ms. Dortch:

On July 22, 2005 Qwest Corporation ("Qwest") filed a petition seeking waiver of the Federal Communications Commission's ("Commission") depreciation prescription process in accordance with the waiver requirements the Commission established in the *USTA Depreciation Order*.¹

On August 3, 2007, Melissa Newman and Phil Grate, in person, and Timothy Boucher, Betty Knapp, Jeromc Miller, Jim Jones and Glenda Weibel, by telephone, all of Qwest, and Jim Hannon, by phone, representing Qwest, met with Al Lewis, Don Stockdale, Deena Shetler, Cindy Spiers, Jay Atkinson, Doug Slotten and Bryan Clopton of the Wireline Competition Bureau regarding the above-captioned waiver proceeding and Qwest's January 30, 2007 amendment to its depreciation rate revisions.

During the meeting, several issues were raised. Qwest responds to these issues in Attachment A and the various additional attachments hereto.

Sincerely,

/s/ Phil Grate

In the Matter of 1998 Biennial Regulatory Review -- Review of Depreciation Requirements for Incumbent Local Exchange Carriers, United States Telephone Association's Petition for Forbearance from Depreciation Regulation of Price Cap Local Exchange Carriers, Report and Order in CC Docket No. 98-137, Memorandum Opinion and Order in ASD 98-91, 15 FCC Rcd 242 (1999) ("USTA Depreciation Order").

ATTACHMENT A

In this attachment Qwest responds to questions that arose during its August 3, 2007 meeting with FCC staff members. Many of the same or similar questions have arisen in past meetings with FCC staff since Qwest first filed its waiver petition on July 22, 2005. Frequently, Qwest has responded to such questions in written *ex partes*. In order to avoid repetition and for the FCC staff's convenience, Qwest is attaching copies of these prior filings as additional attachments to this *ex parte*.

SFAS 143

Questions

Numerous questions arose with respect to Qwest's application of SFAS 143 to its regulated operations, after a grant of Qwest's waiver petition, including: 1) whether SFAS 143 is inconsistent with the Commission's Part 32 accounting rules; 2) whether it should be a concern that SFAS 143 was released after the Commission adopted its waiver requirements in the *USTA Depreciation Order*; and 3) whether implementing SFAS 143 would allow Qwest to "double recover" the cost of telephone plant.

Response

SFAS 143 v. Part 32

There has never been any question that SFAS 143 conflicts with the Commission's Part 32 rules.² Under SFAS 143, the normal cost of removal is charged to expense (*i.e.*, at the time of removal)³ while the Part 32 rules basically require that the cost of removal (less

¹ In the Matter of 1998 Biennial Regulatory Review – Review of Depreciation Requirements for Incumbent Local Exchange Carriers, United States Telephone Association's Petition for Forbearance from Depreciation Regulation of Price Cap Local Exchange Carriers, Report and Order in CC Docket No. 98-137, Memorandum Opinion and Order in ASD 98-91, 15 FCC Rcd 242 (1999) ("USTA Depreciation Order").

Thus, it is not surprising that the Commission found that SFAS 143 "would conflict with the Commission's current accounting rules" and notified carriers that they should not adopt SFAS 143 for federal regulatory accounting purposes. See In the matter of Statement of Financial Accounting Standards Board. Statement of Financial Accounting Standards No. 143, Accounting for Asset Retirement Obligations, Order. 17 FCC Rcd 25552, 25552 \$2 (2002). Clearly, in order for a company to adopt SFAS 143 for regulatory purposes either a rule change, forbearance or a waiver would be required. However, it should be noted that in its 1998 Notice of Proposed Rulemaking addressing depreciation, the Commission proposed eliminating net salvage (i.e., salvage less the cost of removal) from the depreciation prescription process. See In the Matter of 1998 Biennial Regulatory Review -- Review of Depreciation Requirements for Incumbent Local Exchange Carriers, Notice of Proposed Rulemaking, 13 FCC Rcd 20542, 20548 \$9 (1998). If the Commission had acted on this proposal, it would have eliminated the current conflict between SFAS 143 and the Part 32 rules.

³ To the extent that a legal obligation exists to remove an asset, SFAS 143 requires that the fair value of the obligation be capitalized as part of the carrying value of the asset and depreciated over the remaining life of the asset.

the salvage value) be depreciated over the life of the equipment.⁴ Qwest acknowledged this conflict in its waiver petition and requested that the Commission waive 47 C.F.R. §§ 32.2000(g)(2)(ii) and 32.3100(c) in order to allow Qwest to adjust its regulatory books to agree with its financial books.⁵ As Qwest notes in its petition, this was necessary to satisfy the Commission's first waiver condition (requiring a carrier to adjust the net book costs on its regulatory books to the level currently reflected in its financial books by a below-the-line write-off). Also, in order to comply with the second waiver condition (requiring that carriers use the same depreciation factors and rates for both regulatory and financial accounting purposes), Qwest must implement SFAS 143 for regulatory purposes.

Timing of Release of SFAS 143

The fact that SFAS 143 was released after the Commission adopted its depreciation waiver requirements in the *USTA Depreciation Order* should not be a concern. The *USTA Depreciation Order* does not set forth specific Part 32 accounting rules that would be waived or the specific rules that price cap LECs would be required to follow after grant of a waiver. Instead, the Commission concluded that it would be appropriate to grant a waiver of its "depreciation prescription process" for a price cap LEC if the LEC, voluntarily, satisfied certain specific conditions. In adopting these waiver conditions in its *USTA Depreciation Order*, the Commission was well-aware of the possibility that SFAS 143 and other Statement of Financial Accounting Standards under consideration might be adopted. The fact that the Commission established conditions that must be satisfied prior to the grant of a waiver -- rather than identifying specific rules to be waived -- provides sufficient flexibility to accommodate continuing changes in GAAP. As such, the fact that the *USTA Depreciation Order* preceded the adoption of SFAS 143 does not present a problem and should not be an issue.

⁴ 47 C.F.R. § 32.2000(g)(2)(ii) requires companies to account for the estimated cost of asset retirements as part of the net salvage estimates included in the calculation of depreciation rates. Actual incurred costs associated with the cost of removal are charged to Account 3100(c).

⁵ Qwest Waiver Petition at 1-3, 9 and Declaration of R. William Johnston at Attachment C. As Mr. Johnston states in his declaration, "Qwest's proposed waiver request incorporates the effects of numerous statements of Financial Accounting Standards ("SFAS") and Generally Accepted Accounting Principles ("GAAP") that have not been adopted for federal regulatory accounting purposes including SFAS Nos. 142, 143 and 144." Johnston Declaration at 1. Also see, letters from Ed Henry, Director - Finance. Qwest to Marlene Dortch, Secretary, Federal Communications Commission, dated April 12, 2006 (see Attachment C), June 1, 2006 (see Attachment D) and October 4, 2006 (see Attachment E).

[&]quot;Specifically, we find that such a waiver may be approved when an incumbent LEC, voluntarily, in conjunction with its request for waiver: (1) adjusts the net book costs on its regulatory books to the level currently reflected in its financial books by a below-the-line write-off; (2) uses the same depreciation factors and rates for both regulatory and financial accounting purposes; (3) foregoes the opportunity to seek recovery of the write-off through a low-end adjustment, an exogenous cost adjustment, or an above-cap filing; and (4) agrees to submit information concerning its depreciation accounts, including forecast additions and retirements for major network accounts and replacement plans for digital central offices. Finally, the waiver request must comply with section 1.3 of the Commission's rules." *USTA Depreciation Order*, 15 FCC Rcd at 252-53 ¶ 25 (footnotes omitted).

⁷ See id. at 250-51 ¶¶ 20-21.

Questions about potential "double recovery"

The implementation of SFAS 143 for regulatory purposes at the federal level, after a grant of Qwest's waiver petition, will **not** result in "double recovery" of telephone plant. This is true for several reasons. To begin with, the concept of "double recovery" presupposes the application of traditional rate base rate-of-return regulation in which rates are established to recover the utility's costs as recorded on its books of account. Under price cap regulation the link between costs and rates is severed. Indeed, the waiver requirements that the Commission adopted in the *USTA Depreciation Order* restrict waivers of the depreciation rules to certain price cap carriers. Thus, using SFAS 143 after the grant of a depreciation waiver can have no effect on a carrier's recovery of costs (including cost of removal). In light of the above, it follows that questions associated with "double recovery" of costs necessarily presuppose a purely hypothetical situation (which does not currently exist and is not likely to exist in the future) in which Qwest is under rate-of-return regulation at the federal level.

Moreover, even assuming that Qwest had never gone under price cap regulation in the federal jurisdiction and that Qwest continued to operate under rate-of-return regulation, the implementation of SFAS 143 for regulatory purposes under the grant of the waiver still would **not** result in "double recovery" of telephone plant costs. To the contrary, under rate-of-return regulation the implementation of the waiver would result in Qwest foregoing recovery of an increment of embedded telephone plant cost equal to the amount of net plant written-off at the time the waiver is implemented. For example, if the waiver were effective February 1, 2007, the amount of net plant for which Qwest would forego recovery would be \$17 million comprised of the following elements?:

⁸ Qwest has had numerous discussions with Commission staff on the issue of how the adoption of SFAS 143 would affect Qwest's regulated books. In particular, in its November 17, 2006 Ex Parte, Qwest directly addressed the possibility of over recovery following the adoption of SFAS 143 and demonstrated that "there is no possibility of over recovery by any carrier in the federal jurisdiction following the adoption of FAS 143 in conjunction with the waiver prescription process." *See*, letter from Melissa Newman, Vice President -Federal Regulatory, Qwest, to Marlene Dortch, Secretary, Federal Communications Commission, dated November 17, 2006 (*see* Attachment F). *Also see*, letters from Ed Henry, Director-Finance, Qwest, to Marlene Dortch, Secretary, Federal Communications Commission, dated December 1, 2005, April 12, 2006 and June 1, 2006 (*see* Attachments G, C, D).

⁹ This example was contained in a letter from Philip E. Grate, Director-State and Federal Relations, Qwest, to Marlene Dortch, Secretary, Federal Communications Commission, dated May 30, 2007 (see Attachment 11). A discussion of each component of the net plant write-off can be found on pages 1 through 3 of the Attachment to this letter.

[Begin Confidential]

SFAS 143 Cost of Removal Amount Parameters and Timing Differences Non-Regulated Accounts Contributions in Aid of Construction Intangibles & Other Total Reserve Differences Investment Differences Total Net Plant Differences



[End Confidential]

In other words, there would effectively be net plant "write-ons" for 1) SFAS 143 Cost of Removal, 2) Non-Regulated Accounts and 3) Investment Differences. If rate-of-return regulation were in effect and one were to look only at these "write-on" components in isolation and ignore the overall effect of the transaction, one might raise the question of whether Qwest would have the opportunity to recover some or all of these "written-on" embedded costs after the implementation of the waiver. However, again, Qwest is not subject to rate-of-return regulation. Additionally, in Qwest's case there would also be "write-offs" of net plant associated with: 1) Parameters and Timing Differences, 2) Contributions in Aid of Construction, 3) Intangibles and Other, and 4) Investment Differences. Under rate-of-return regulation Qwest would forego recovery of these "written-off" costs. ¹⁰ As of February 1, 2007, the amount of "written-off" costs would exceed the amount of "written-on" costs by \$17 million. Thus, even if Qwest were subject to rate-of-return regulation -- which clearly is not the case -- Qwest would have no opportunity to "double recover" its cost of telephone plant because the "write-offs" exceed the "write-ons" described above.

Consequently, if the waiver were effective February 1, 2007, Qwest ratepayers, even if Qwest were under rate-of-return regulation, would receive a net benefit of at least \$17 million because Qwest would be certain to forego any opportunity to recover \$17 million more of cost than it would have an opportunity to "double recover." Attachment B, attached hereto, provides a detailed hypothetical example that further explains and illustrates the accounting and rate-of-return ratemaking concepts that lead to this conclusion.

¹⁰ Under rate-of-return regulation Qwest would be absolutely certain to forego recovery of these costs precisely because they are written-off. Once removed from Qwest's books by the below-the-line write-off, Qwest would no longer have any opportunity to recover them even it the Commission were to subject Qwest to rate-of-return regulation at some time in the future.

It should be noted that the amount of regulated net telephone plant cost recovery Qwest would forego actually exceeds \$17 million because [Begin Confidential] [End Confidential] million of the write-on of net plant is attributable to non-regulated accounts. Consequently, the amount of regulated telephone plant cost recovery Qwest would forego is actually [Begin Confidential] [End Confidential] million (\$17 million plus [Begin Confidential] [End Confidential] million).

Additionally, the Commission can take further comfort from the fact that, in the unlikely event Qwest were subjected to rate-of-return regulation in the future, the Commission would have ample opportunity to identify and take into account any unusually high or low levels of recorded costs in regulated results of operations (including costs of removal recorded as incurred under SFAS 143). Again, Qwest believes that a reversion to rate-of-return regulation is an extremely remote possibility. But, in that unlikely eventuality, it would be necessary for the Commission to conduct a comprehensive cost analysis under rate-of-return ratemaking principles in order to establish rates designed to recover Qwest's costs. This would include an analysis of all relevant costs used to provide regulated services.

Finally, even though the question did not arise in Qwest's August 3, 2007 meeting with Commission staff, it is worth noting that adoption of SFAS 143 for regulatory accounting purposes will not result in "double recovery" of telephone plant costs in Qwest's state jurisdictions. First, accounting for cost of removal is irrelevant except in states that continue to rely on rate-of-return regulation. Except in such states, double recovery of costs is impossible because changes in cost recognition have no effect on rates. Second, all state regulatory commissions retain unfettered authority under the Supreme Court's *Louisiana Public Service Commission* decision to establish the depreciation accounting methods to be followed for intrastate regulatory purposes in their respective states. It follows that any state commission can reject the use of SFAS 143 for regulatory accounting and/or ratemaking purposes regardless of whether Qwest employs it for FCC accounting purposes.

POLE ATTACHMENT RATES

Question

On October 24, 2005, Qwest filed an *ex parte* indicating that Qwest's pole attachment rates would change very little with a grant of Qwest's waiver petition.¹³ Is this statement still true in light of Qwest's December 28, 2006 depreciation rate revisions (and subsequent amendments)?

Response

The statement is still true because Qwest did not change its depreciation rates for account 2411, poles, in its 2006 depreciation rate revisions, as amended.¹⁴

³² See Louisiana Public Service Commission v. FCC, 476 U.S. 355 (1986).

¹³ See letter from Ed Henry. Director -Finance. Qwest to Marlene Dortch, Secretary, Federal Communications Commission, dated October 24, 2005 (see Attachment I).

Qwest previously addressed the effect the waiver would have on pole attachment rates in letters from Ed Henry, Director -Finance, Qwest to Marlene Dortch, Secretary, Federal Communications Commission, dated September 9, 2005 (see Attachment J); October 24, 2005 (see Attachment I); December 1, 2005 (see Attachment G); February 9, 2006 (see Attachment K); March 6, 2006 (see Attachment L) and June 1, 2006 (see Attachment D).

UNES AND UNIVERSAL SERVICE

Question

Wouldn't a grant of Qwest's waiver petition deprive regulators of information necessary for calculating UNE rates and USF support?

Response

No. In the *USTA Depreciation Order*, the Commission indicated that it would "continue to maintain realistic ranges of depreciable life and salvage factors for each of the major plant accounts." In this *Order*, the Commission recognized the importance of depreciation rates in calculating high-cost support and UNE rates. The Commission concluded that its four waiver conditions were sufficient to "guard against adverse impacts on consumers and competitors" and to "prevent any inappropriate and undesirable fluctuations in high cost support or the rates for interconnection and UNEs due to changes in depreciation rates by carriers receiving a waiver..." The Commission was able to reach this determination because neither the development of UNE rates nor USF support calculations relies on individual company depreciation rates or depreciation records.

ACCOUNT 2311

Question

In Qwest's August 2, 2007 ex parte¹⁹ in the confidential attachment entitled "Net Book Detail," why is the Financial Reporting (FR) balance in account 2311, Station Apparatus,

¹⁵ USTA Depreciation Order, 15 FCC Rcd at 257 ¶ 34.

¹⁶ *Id.* at 255-58 ¶¶ 29-35.

¹⁷ "Thus, in order to prevent inappropriate and undesirable fluctuations in high cost support or the rates for interconnection and UNEs due to changes in depreciation rates caused by carriers receiving a waiver, we will continue to maintain realistic ranges of depreciable life and salvage factors for each of the major accounts. These ranges can be relied upon by federal and state regulatory commissions for determining the appropriate depreciation factors to use in establishing high cost support and interconnection and UNE prices. ... This condition [the Commission's information submission requirement] will assure that any increase in depreciation expense will not have a harmful effect on consumers or competition in rates calculated using reported costs or forward-looking cost models." Id. at 257 ¶ 34.

¹⁸ With regard to the calculation of Universal Service High Cost Support see Federal State Joint Board on Universal Service, CC Docket No. 96-45, Ninth Report & Order and Eighteenth Order on Reconsideration, FCC 99-306 (rel. Nov. 2, 1999) and Federal State Joint Board on Universal Service, Forward-Looking Mechanism for High-Cost Support for Non-rural LECs, CC Dockets Nos. 96-45, 97-160, Report & Order, FCC 99-304 (rel. Nov. 2, 1999).

¹⁹ Letter from Philip E. Grate, Director --State and Federal Relations, to Marlene Dortch, Secretary, Federal Communications Commission, dated August 2, 2007 (see Attachment M).

for column "b" (entitled "Reserve") a debit when all other balances in column "b" are either zero or a credit?

Response

Account 2311 is a component account of the rate category "Other Terminal Equipment" which also includes account 2362. For Financial Reporting (FR) purposes Qwest reports the rate category, not the individual accounts that comprise it. Consequently, Qwest does not report account 2311. Station Apparatus, separately in its external financial reports.

For FR accounting purposes, Qwest records depreciation **expense** to the accumulated depreciation account ("reserve") of only the largest plant account within a rate category. Consequently, Qwest records all depreciation expense for the rate category "Other Terminal Equipment" to the reserve for account 2362. For FR accounting purposes, Qwest records no depreciation expense to the reserve for account 2311. However, Qwest debits retirement transactions to each individual plant account. So retirements in account 2311 are debited to the reserve for account 2311 and retirements in account 2362 are debited to the reserve for account 2362.

Because retirement transactions booked to the reserve for account 2311 are debits, and because no depreciation expense is booked (credited) to the reserve for account 2311, it has a debit balance which is reflected in column "b" of the attachment entitled "Net Book Detail" to Qwest's August 2, 2007 ex parte. If accounts 2311 and 2362 were combined on the "Net Book Detail" attachment (as they are for FR reporting purposes) the resulting reserve would have a normal (i.e., credit) balance. Specifically, the investment balance would be a debit of [Begin Confidential] [End Confidential] [End Confidential].

ACCUMULATED DEPRECIATION RESERVES

Question

Why are some of Qwest's depreciation reserves on its FCC books in excess of service value?

Response

As of January 1, 2006, Qwest's reserves exceeded service value²¹ in a total of 51 different accounts spread across Qwest's 14 states.²² In total, the amount of reserves in excess of

²⁰ Id.

²¹ In depreciation accounting, the term "service value" is the amount of depreciation required to fully depreciate the investment in an account. It is an amount equal to 100% (*i.e.*, gross investment) plus the cost of removal percentage less the salvage percentage multiplied by gross investment.

²² Additionally, it should be noted that as of January 1, 2006, Qwest had reserve deficiencies that largely offset these excess reserves.

service value was \$60.0 million.²³ However, it should also be noted that the depreciation rate changes that Qwest filed in this proceeding did not give rise to depreciation reserves in excess of service value. The excess reserves existed on January 1, 2006, before the effect of Qwest's depreciation rate revisions.

A variety of factors that preceded Qwest's 2006 depreciation rate revisions contributed to the existence of excess reserves. Qwest's excess reserves were largely due to the following reasons: 1) transfers between accounts;²⁴ 2) the effect of transferring assets from jurisdictions with higher service value ratios to jurisdictions with lower service value ratios; 3) the timing of when depreciation accruals are "turned-off" for different investment accounts; and 4) the timing of the receipt of salvage and the incurrence of cost of removal.

Of the \$60.0 million of excess reserves as of January 1, 2006, \$30.15 million was in reserves for account 2232. Circuit Analog, in 13 states. These excesses arose when Qwest transferred assets from Circuit Analog accounts to other accounts. A large part of excess reserves associated with account 2232 was the result of a Qwest error which was discovered in May 2007 and subsequently corrected. Another \$24.65 million of the total excess reserve as of January 1, 2006 was in the reserves of account 2124, General Purpose Computers, in five states. These excesses arose in 2003 and 2004 and were the result of the timing of when depreciation accruals were "turned-off" for this account in these states. Qwest reviews its reserve levels quarterly and discontinues recording depreciation at the end of any quarter in which the reserve level is at or above service value. In these five states, the reserve levels grew beyond service value in-between quarterly reviews. When the excesses first arose, they totaled [Begin Confidential]

²³ Qwest notes that as of August 1, 2007, only 34 of these accounts were over service value by a total of **|Begin Confidential| End Confidential|** million.

When a carrier transfers an asset from one account to another, it transfers the gross investment in the asset and an associated increment of depreciation reserve. Because Qwest uses mass asset accounting for depreciation (and, therefore, does not keep depreciation records on individual assets), the amount of depreciation reserve to be transferred must be calculated. This calculation uses a ratio of the amount of the gross investment in the account to the amount of the reserve for the account (reserve ratio).

²⁵ In transferring Circuit Analog equipment, Qwest's depreciation system erroneously used a reserve ratio for Circuit DDS instead of the reserve ratio for Circuit Analog. The reserve ratio for Circuit DDS was smaller than the reserve ratio for Circuit Analog. Consequently, when Qwest transferred Circuit Analog equipment, the amount of reserve transferred with it was less than it should have been. The insufficiency left more reserve in the Circuit Analog accounts than there should have been. Qwest discovered this error during a review of the excess reserves in Circuit Analog in May 2007 and recorded correcting entries in June 2007.

COMPARABILITY OF DEPRECIATION DATA

Question

Won't a grant of Qwest's depreciation waiver make it more difficult to compare industry depreciation data?

Response

No more so than it already is. First and foremost, it must be acknowledged that only a small number of telecommunications service providers are subject to the Commission's depreciation rules. Under current FCC rules, the Commission does not prescribe depreciation for LECs except for dominant incumbent LECs with annual operating revenues of \$134 million or more. CLECs, IXCs, cable companies, wireless companies, VoIP providers and other telecommunications service providers are not subject to the Commission's depreciation regulations. Therefore, comparing Qwest's regulated depreciation data with the data available from a small subset of all the companies that provide telecommunications services in the United States is unlikely to provide any useful information for Commission policy setting purposes.

Furthermore, since the adoption of price cap regulation for the largest ILECs in 1991, there has been much less need for the Commission to review depreciation data and this has been reflected in fewer Commission prescriptions and other orders affecting depreciation rates. In 1994 the Commission established basic factor ranges (*i.e.*, life and salvage factor ranges) for 22 plant categories.²⁷ In 1995 the Commission adopted values for the basic factor ranges for eight additional plant categories and simplified procedures for the remaining categories.²⁸ Since then, the Commission has updated a value for a basic factor range for only one plant category, digital switches, and that was almost eight years ago.²⁹ The Commission last issued a depreciation prescription order for Qwest nearly ten years ago.³⁰ The Commission last issued a depreciation prescription order for any LEC in August of 2000.³¹ So far as Qwest is aware, no carrier except Qwest has reported revised depreciation rates under 47 C.F.R. § 43.43(c) in this decade.

²⁶ See 47 C.F.R. §§ 43.43(a) and 32.9000.

²⁷ In the Matter of Simplification of the Depreciation Prescription Process, Second Report and Order, 9 FCC Red 3206, 3209 ¶ 24-25 (1994).

²⁸ In the Matter of Simplification of the Depreciation Prescription Process, Third Report and Order, 10 FCC Red 8442, 8444 ¶ 5 (1995).

²⁹ USTA Depreciation Order, 15 FCC Red at 247-48 ¶ 13.

³⁶ In the Matter of Cincinnati Bell Telephone Company, Southwestern Bell Telephone Company, and US WEST Communications, Inc., Prescription of Revised Depreciation Rates, Memorandum Opinion and Order, 13 FCC Rcd 6221 (1998) ("Depreciation MO&O").

³⁴ The most recent depreciation prescription the Commission has issued for any LEC was released in August of 2000, for Verizon Hawaii & Verizon Northwest. See In the Matter of The Prescription of

The almost complete absence of significant Commission and industry activity with regard to depreciation accounting for so many years casts a deep shadow of doubt on the need for the Commission to continue to regulate the depreciation processes of a small number of companies. The longstanding inattention to regulatory depreciation accounting renders the carriers' financial reports a more consistent and a far more comprehensive source of depreciation information, because they are issued on a consistent basis (GAAP) by all providers of telecommunications services.³²

Even with a grant of Qwest's petition, Qwest will be required to submit "certain information about network retirement patterns and modernization plans related to their plant accounts so that we [the Commission] can maintain realistic ranges of depreciable life and salvage factors for each of the major plant accounts."³³

ACCOUNTS 2212, 2232 AND 2423

Question

Assuming Qwest had not changed its depreciation rates on its FCC books effective January 1, 2006, what explains the differences in net plant balances between Qwest's FCC books and its Financial Reporting ("FR") books as of January 1, 2007 for Qwest's three largest plant accounts -- Accounts 2212-digital switched equipment, 2232-circuit and 2423-buried cable?

Response

If Qwest had not revised its depreciation rates in 2006, the differences as of January 1, 2007 between Qwest's FCC books and its FR books for accounts 2212 and 2232 would have been almost exclusively due to parameter³⁴ differences and timing differences³⁵ associated with Qwest's FCC and FR depreciation rates. Qwest changes its FR (*i.e.*, GAAP) depreciation rates annually to reflect the effect of the passage of time on remaining life calculations and reserve levels and to update lives and survivor curves. Prior to its 2006 depreciation rate revision, Qwest's most recent FCC depreciation rate change occurred in 1998 in conjunction with the triennial depreciation review process.³⁶

Revised Percentages of Depreciation pursuant to the Communications Act of 1934, as amended for: Verizon Hawaii, Incorporated, Verizon Northwest, Incorporated, Memorandum Opinion and Order, 15 FCC Red 16214 (2000).

³² Companies' financial reports are filed with the Securities and Exchange Commission and are subject to the strictures of GAAP and Sarbanes Oxley and the scrutiny of annual audit by independent auditors.

³³ USTA Depreciation Order, 15 FCC Rcd at 256 ¶ 31.

¹⁴ Depreciation parameters are estimates used in the development of depreciation rates. There are three "parameters" that are used in the depreciation rate calculation; the estimated life, the estimated survivor pattern (Curve Shape) and an estimate of future net salvage.

³⁵ "Timing differences" refer to how frequently Qwest changes its FCC and FR depreciation rates.

³⁶ See Depreciation MO&O, 13 FCC Rcd 6221.

For account 2423, buried cable, approximately 65% of the difference would have been due to differences between the treatment of the cost of removal on Qwest's FCC books and its FR books (*i.e.*, the impact of SFAS 143) and 35% would have been due to parameter and timing differences.

Rate-of-Return Hypothetical Example

Assuming *arguendo*, that Qwest were still subject to traditional rate base rate-of-return regulation at the federal level and such rate-of-return regulation continued after a grant of the waiver, it still would not be possible for Qwest to double recover the embedded cost of its telephone plant provided that Qwest records a below-the-line write-off of net plant in order to comply with waiver condition (1). Following is a discussion of a hypothetical example to illustrate this point.

For purposes of this example, the following facts are assumed:³

	Part 32	GAAP
Gross investment in plant	\$1,200	\$1,200
Estimated total salvage value of plant	\$42	\$42
Estimated total cost of removal of plant	\$180	\$180
Estimated average life of plant	6 years	5 years

With these assumed facts the depreciation expense recorded under Part 32 and resulting net plant are as follows.

Part 32 Schedule of Depreciation Expense	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Total
Depr Exp attributable to gross investment	\$200	\$200	\$200	\$200	\$200	\$200	\$1,200
Depr Exp attributable to salvage value	(\$7)	(\$7)	(\$7)	(\$7)	(\$7)	(\$7)	(\$42)
Depr Exp attributable to cost of removal	\$30	\$30	\$30	\$30	\$30	\$30	\$180
Total Depreciation Expense	\$223	\$223	\$223	\$223	\$223	\$223	\$1,338
					•		
Gross investment in plant	\$1,200	\$1,200	\$1,200	\$1,200	\$1,200	\$1,200	
Accumulated Depreciation	\$223	\$446	\$669	\$892	\$1,115	\$1,338	
Net Plant (Gross Investment - Acc Depr)	\$977	\$754	\$531	\$308	\$85	(\$138)	

Note that at the end of year six and before removal of the plant, the total depreciation expense and the balance in the accumulated depreciation account in the hypothetical example are both \$1,338 even though gross investment in plant is only \$1,200. This is because under Part 32, \$180 of depreciation expense has been accrued for the estimated

¹ Qwest reiterates that this example is purely hypothetical and that an ILEC must be subject to price cap regulation in order to qualify for a waiver under the Commission's *USTA Depreciation Order*.

² Waiver condition (1) is that the ILEC, voluntarily, in conjunction with its request for waiver "adjusts the net book costs on its regulatory books to the level currently reflected in its financial books by a below-the-line write-off."

³ This example relies on a set of assumed facts similar to those at paragraph 13 of the *Depreciation NPRM*. See In the Matter of 1998 Biennial Regulatory Review -- Review of Depreciation Requirements for Incumbent Local Exchange Carriers, Notice of Proposed Rulemaking, 13 FCC Red 20542, 20550 ¶ 13 (1998) (Depreciation NPRM).

Rate-of-Return Hypothetical Example

cost of removal and \$42 of negative depreciation expense has been accrued for the estimated salvage value. If and when the plant is removed, the salvage received will be credited to the accumulated depreciation account and the cost of removal will be charged to the accumulated depreciation account as shown below.

	Balance	Gross	Cost of	Total
	at end of	Salvage	Removal	after
	Year 6	Received	Paid	Removal
Gross investment in plant	\$1,200			\$1,200
Accumulated Depreciation	\$1,338	\$42	(\$180)	\$1,200
Net Plant (Gross Investment - Acc Depr)	(\$138)	(\$42)	\$180	\$0

In the unlikely event (but as assumed in the hypothetical example above) the salvage received and the actual cost of removal are exactly as estimated, the net plant balance will be zero. If not, the net plant balance will almost certainly be something more or less than zero. One of the inherent weaknesses of accrual accounting for salvage and cost of removal is the fact that it is based on estimates that are almost inevitably inaccurate.

By comparison, and with the same assumed facts as described above, the depreciation expense recorded under GAAP and resulting net plant are as follows:

Year 1	Year 2	Year 3	Year 4	Year 5	Total
\$240	\$240	\$240	\$240	\$240	\$1,200
\$0	\$0	\$0	\$0	\$0	\$0
\$0	\$0	\$0	\$0	\$0	\$0
\$240	\$240	\$240	\$240	\$240	\$1,200
\$1,200	\$1,200	\$1,200	\$1,200	\$1,200	
\$240	\$480	\$720	\$960	\$1,200	
\$960	\$720	\$480	\$240	\$0	
	\$240 \$0 \$0 \$240 \$1,200 \$240	\$240 \$240 \$0 \$0 \$0 \$0 \$240 \$240 \$1,200 \$1,200 \$240 \$480	\$240 \$240 \$240 \$0 \$0 \$0 \$0 \$0 \$0 \$0 \$0 \$240 \$240 \$240 \$1,200 \$1,200 \$1,200 \$240 \$480 \$720	\$240 \$240 \$240 \$0 \$0 \$0 \$0 \$0 \$0 \$0 \$0 \$0 \$240 \$240 \$240 \$1,200 \$1,200 \$1,200 \$240 \$480 \$720 \$960	\$240 \$240 \$240 \$240 \$240 \$0 \$0 \$0 \$0 \$0 \$0 \$0 \$0 \$0 \$0 \$240 \$240 \$240 \$240 \$240 \$1,200 \$1,200 \$1,200 \$1,200 \$1,200 \$240 \$480 \$720 \$960 \$1,200

Note that under GAAP, no depreciation expense is accrued for the estimated cost of removal and no negative depreciation expense is accrued for the estimated salvage value. When plant is removed, the salvage received will be credited to maintenance expense and the cost of removal will be charged to maintenance expense.

To continue the hypothetical example, it is assumed that at the end of year three the carrier implements a waiver of the Commission's depreciation prescription process and converts from Part 32 accounting to GAAP accounting, including SFAS 143. It is further assumed that under SFAS 143, no accruable asset retirement obligation (ARO) exists and, therefore, no accrual for cost of removal is warranted.

Rate-of-Return Hypothetical Example

The following schedule sets forth a hypothetical example in which the carrier, in compliance with waiver condition (1) records a \$51 below-the-line net plant write-off in order to make its gross investment and accumulated depreciation balances after implementation of the waiver the same as they are for GAAP purposes.

	FCC Book Balance at end of year three immediately before Waiver implementation	Below-the-Line Write-off at time of Waiver implementation	FCC and GAAP Book Balance immediately after Waiver implementation
Gross Investment	\$1,200.00		\$1,200.00
Accumulated depreciation associated with Gross Investment	\$600.00	\$120.00	\$720.00
Accumulated Depreciation associated with salvage value	(\$21.00)	\$21.00	\$0.00
Accumulated Depreciation associated with Cost of Removal	\$90.00	(\$90.00)	\$0.00
Total Accumulated Depreciation	\$669.00	\$51.00	\$720.00
Net Plant (Gross Investment less Total Accumulated Depreciation)	\$531.00	(\$51.00)	\$480.00

In this hypothetical example, the three elements of the \$162 net plant write-off are as follows:

\$120 not plant "write-off" associated with depreciation on gross investment \$21 net plant "write-off" associated with negative depreciation for salvage \$90 net plant "write-on" associated with depreciation for cost of removal

The following table compares the amount of cost recovery opportunity the carrier is presumed to have under rate-of-return regulation under the baseline assumption that Part 32 is effective for all six years and under the assumption that the waiver is granted at the end of year three with a \$51 below-the-line net plant write-off.

Rate-of-Return Hypothetical Example

Cost Recovery under Part 32	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Re- moval	Total
Depreciation attributable to gross investment	\$200	\$200	\$200	\$200	\$200	\$200	mo rai	\$1,200
Depreciation attributable to salvage value	(\$7)	(\$7)	(\$7)	(\$7)	(\$7)	(\$7)		(\$42)
Depreciation attributable to cost of removal	\$30	\$30	\$30	\$30	\$30	\$30		\$180
Cost recovery opportunity	\$223	\$223	\$223	\$223	\$223	\$223	\$0	\$1,338
	Year	Year	Year	Year	Year		Re-	
Cost Recovery with Waiver at end of Year 3	1	2	3	4	5		moval	Total
Depreciation attributable to gross investment	\$200	\$200	\$200	\$240	\$240			\$1,080
Depr or Maint Exp attributable to salv value	(\$7)	(\$7)	(\$7)	\$0	\$0		(\$42)	(\$63)
Depr or Maint Exp attributable to COR	\$30	\$30	\$30	\$0	\$0		\$180	\$270
Cost recovery opportunity	\$223	\$223	\$223	\$240	\$240		\$138	\$1,287

The schedules show that the cost recovery opportunity under the Part 32 scenario is \$1,338 while the cost recovery opportunity under the waiver scenario is only \$1,287. Thus, the waiver scenario represents a net of \$51 less cost recovery opportunity than does the Part 32 scenario. The components of the \$51 difference are set forth in the following schedule.

	Cost Recovery Opportunity Under Waiver Scenario	Cost Recovery Opportunity Under Part 32 Scenario	Cost Recovery Opportunity Difference
Depreciation attributable to gross investment	\$1,080	\$1,200	(\$120)
Depr or Maint Exp attributable to salvage value	(\$63)	(\$42)	(\$21)
Depr or Maint Exp attributable to cost of removal	\$270	\$180	\$90
Cost recovery opportunity under cost-of-service	\$1,287	\$1,338	(\$51)

The schedule shows that, notwithstanding the \$90 "write-on" of net plant associated with the cost of removal, it is not possible -- even under rate-of-return-regulation -- for the carrier to double recover the embedded cost of its telephone plant because it has recorded a \$51 below-the-line write-off of net plant in compliance with waiver condition (1).

ATTACHMENT C



Qwest 607 14th Street, NW, Suite 950 Washington, DC 20005 Phone 202-429-3122

Ed Henry

EX PARTE

FILED VIA ECFS

April 12, 2006

Ms. Marlene H. Dortch Secretary Federal Communications Commission Room TW B-204 445 12th Street, S.W. Washington, DC 20554

Re:

In the Matter of Petition of Owest Corporation for Waiver of Depreciation Regulation

Pursuant to 47 C.F.R. § 1.3 – WC Docket No. 05-259

Dear Ms. Dortch:

On July 22, 2005 Qwest Corporation ("Qwest") filed a petition seeking waiver of the Federal Communications Commission's ("Commission") depreciation prescription process in accordance with the waiver requirements the Commission established in the USTA Depreciation Order. The purpose of this letter is to address certain issues that might arise during the Commission's further consideration of Qwest's petition. First, why Qwest has requested waiver of sections of the Part 32 rules in addition to those sections that specifically apply to Qwest's depreciation rates, methods and practices. A related issue is whether the relief that Qwest is requesting is broader than that contemplated by the Commission in the USTA Depreciation Order (i.e., when it established the conditions that must be met by price cap carriers in order for the Commission to waive its depreciation prescription process). Second, how can allowing Qwest to adopt Statements of Financial Accounting Standards ("SFAS") 142, 143 and 144 for regulatory accounting purposes be reconciled with the Commission's existing Part 32 rules and Orders. These SFASs were issued after the Commission's USTA Depreciation Order and the

In the Matter of 1998 Biennial Regulatory Review – Review of Depreciation Requirements for Incumbent Local Exchange Carriers, United States Telephone Association's Petition for Forbearance from Depreciation Regulation of Price Cap Local Exchange Carriers, Report and Order in CC Docket No. 98-137, Memorandum Opinion and Order in ASD 98-91, 15 FCC Rcd 242 (1999) ("USTA Depreciation Order").

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Commission subsequently issued *Orders* on SFASs 143 and 144 instructing carriers not to adopt these SFASs because they conflicted with the Part 32 accounting rules.²

USTA Depreciation Order

Qwest's waiver petition is limited to the relief necessary to satisfy the conditions that the Commission established in the USTA Depreciation Order and no more.³ The USTA Depreciation Order does not identify the specific rules that would be waived if a price cap local exchange carrier ("LEC"), such as Qwest, satisfied the Commission's waiver conditions. Instead, the Commission generally refers to granting a waiver of its "depreciation prescription process" and focuses on the specific conditions that must be satisfied.⁴

Specifically, we [the Commission] find that such a waiver may be approved when an incumbent LEC, voluntarily, in conjunction with its request for waiver: (1) adjusts the net book costs on its regulatory books to the level currently reflected in its financial books by a below-the-line write-off; (2) uses the same depreciation factors and rates for both regulatory and financial accounting purposes; (3) foregoes the opportunity to seek recovery of the write-off through a low-end adjustment, an exogenous cost adjustment, or an above-cap filing; and (4) agrees to submit information concerning its depreciation accounts, including forecast additions and retirements for major network accounts and replacement plans for digital central offices. [Footnotes omitted.]⁵

Thus, rather than identifying specific rules, the Commission established specific requirements that must be satisfied for waiver -- implying that all rules necessary to satisfy these conditions would be waived in addition to all rules specifically addressing the Commission's depreciation

In the matter of Financial Accounting Standards Board, Statement of Financial Accounting Standards No. 143. Accounting for Asset Retirement Obligations, Order, 17 FCC Red 25552 (2002) ("FASB 143 Order"); In the matter of Financial Accounting Standards Board, Statement of Financial Accounting Standards No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets, Order, 18 FCC Red 10005 (2003) ("FASB 144 Order").

⁸ USTA Depreciation Order, 15 FCC Rcd at 245-59 ¶ 7-40. Also see, In the Matter of 1998 Biennial Regulatory Review - Review of Depreciation Requirements for Incumbent Local Exchange Carriers, Ameritech Corporation Telephone Operating Companies' Continuing Property Records Audit, et al., GTE Telephone Operating Companies Release of Information Obtained During Joint Audit, Second Report and Order in CC Docket No. 99-173 and Order in CC Docket No. 99-173 and AAD File No. 98-26, 16 FCC Rcd 4083, 4086-87 ¶ 6-7 (2000), which reaffirmed the Commission's requirements for a depreciation waiver and rejected an alternative proposal.

⁴ USTA Depreciation Order, 15 FCC Red at 252-53 ¶ 25.

⁵ *Id.*

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prescription process. That is why Qwest's petition has the appearance of being broader than a request for waiver of the Commission's "specific" depreciation rules. However, Qwest's petition does not ask for waiver of any additional Part 32 rules other than those necessary to satisfy the Commission's requirements in the *USTA Depreciation Order* (i.e., conditions (1)-(4) quoted above).

Of particular importance in identifying the specific Part 32 rules that need to be waived in order to satisfy the Commission's waiver requirements is condition (1), above, which requires that net book cost be the same on both a carrier's regulatory and financial books. Qwest identified the rules necessary to satisfy condition (1) in prior ex partes. These rules are listed in the attached table. Without waiver of these sections it is impossible to satisfy the Commission's requirement that net book cost be the same on Qwest's regulated and financial books at the time of the waiver and going forward.

Of equal importance, is the Commission's requirement that a LEC use the same depreciation factors and rates for both regulatory (*i.e.*, Part 32) and financial accounting purposes (*i.e.*, condition (2) above) going forward. While this requirement would appear to be self-evident in any waiver of the Commission's depreciation prescription process, it does have significant implications regarding the scope of the Part 32 rules that need to be waived, as noted below.

SFAS 142

The Commission has not issued an order concerning adoption of SFAS 142 on LECs' regulated books nor is Qwest aware of any LEC requesting that it be allowed to adopt SFAS 142 for regulatory accounting purposes. SFAS 142 addresses how goodwill and other intangible assets that are acquired are accounted for on a company's financial books. There is no question that SFAS 142 directly conflicts with Part 32. Section 32.2007 requires amounts identified as "goodwill" to be amortized on a straight-line basis over the remaining life of the acquired plant while SFAS 142 does not allow goodwill to be amortized but requires that it be evaluated annually for possible impairment." Despite this conflict between SFAS 142 and Part 32, it is of little, if any, importance at the present with regard to Qwest's pending waiver because Qwest (i.e., Qwest Corporation, the regulated entity) does not have any goodwill on its books. As such, Qwest is not amortizing goodwill in accordance with Section 32.2007 nor will it be

See ex parte letters from Ed Henry, Qwest, to Ms. Marlene H. Dortch, Federal Communications Commission, WC Docket No. 05-259, dated April 5, 2006 and August 12, 2005.

² A continuing waiver of these sections is necessary to ensure that net book costs remain in agreement going forward.

⁶ 47 C.F.R. § 32.2007.

Statement of Financial Accounting Standards No. 142 at 6 and 12, http://www.fasb.org/pdf/fas142.pdf.

¹⁶ See Qwest petition at n.11.

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evaluating any goodwill amounts for impairment, as is required by SFAS 142, if Qwest's waiver is granted. However, waiver of Section 32.2007 is necessary to ensure that net book costs on Qwest's regulated books continue to agree with its financial books going forward. Furthermore, waiver of this rule eliminates any potential conflict between SFAS 142 and Part 32.

SFAS 143 and 144

The Commission has issued *Orders* finding that SFAS 143 and 144 conflicted with its Part 32 accounting rules and notified carriers that they "shall not" adopt these SFASs for federal regulatory accounting purposes "unless the Commission specifically requires adoption" of SFAS 143 and 144 in the future.¹¹

SFAS 143 conflicts with Part 32 in the following ways. Section 32.2000(g)(2)(ii) requires companies to account for the cost of asset retirements as part of net salvage estimates included in the calculation of depreciation rates while costs associated with cost of removal are charged to Account 3100(c). Under SFAS 143, the normal cost of removal is charged to expense. In addition, to the extent that a legal obligation exists to remove an asset, SFAS 143 requires that the fair value of the obligation be capitalized as part of the carrying value of the asset and depreciated over the remaining life of the asset. SFAS 143 effectively lowers depreciation rates going forward but results in higher expenses since the cost of removing an asset will be expensed at the time of removal (and will no longer be included in depreciation rates). Thus waiver of Section 32.2000(g)(2)(ii) is necessary if Qwest is going to comply with condition (2) above and use the same depreciation rates for regulatory and financial accounting purposes.

Under SFAS 143, cost of removal and any other retirement obligations will be recognized when they are incurred. Qwest's overall costs will not change with the adoption of SFAS 143 — it is simply a timing difference. By far, the largest impact of SFAS 143 will be the one-time adjustment at the date of adoption.¹³ However, waiver of Sections 32.2000(g)(2)(ii) and 32.3100(c) is necessary if Qwest is going to keep net book cost on its regulated books in agreement with its financial books.

"SFAS No. 144 requires companies to recognize an impairment loss when the carrying value of an asset is not recoverable from undiscounted cash flows" while Section 32.2000(d)(1) requires

¹¹ SFAS 143 Order, 17 FCC Red at 25553 ¶ 4; SFAS 144 Order, 18 FCC Red at 10005-06 ¶ 4.

¹² See 47 C.F.R. § 32.3100(c).

In an earlier ex parte, Qwest provided the Commission with a detailed example of the estimated impact that the one-time adjustment would have on each of the affected plant accounts. See ex parte letter from Ed Henry, Qwest, to Ms. Marlene H. Dortch, Federal Communications Commission, WC Docket No. 05-259, dated September 9, 2005.

^{**} SFAS 144 Order, 18 FCC Rcd at 10005 ¶ 1.